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To our Clients and Other Friends:

We are writing to bring to your attention a number of matters that may bear on your estate planning or on the estate planning of others to whom you provide advice and guidance.

The federal estate and generation-skipping transfer taxes were repealed as of January 1, 2010. Consequently, unless Congress acts to undo that repeal, no federal estate tax will apply to estates of individuals dying in 2010 and no generation-skipping transfer tax will apply to transfers made during 2010. Although the federal gift tax remains in effect, the highest applicable tax rate was decreased from 45% to 35% for gifts made during 2010.

As the law now stands, the federal estate and generation-skipping transfer taxes will return on January 1, 2011, with the rates (up to 55%, increased from the 45% rate in 2009) and exemptions ($1,000,000, down from the $3,500,000 exemption in 2009) that would have applied under 2001 law. However, we expect Congress will change the law sometime in 2010 in a way that brings back these taxes sooner, possibly with retroactive effect so that they apply as of January 1, 2010.

We are in a highly uncertain environment with respect to these taxes. It is not clear whether or when Congress will change the law in 2010, what changes may be made, or whether any changes will take effect as of the date of the new law or as of January 1, 2010 (thereby eliminating the current "tax-free" window). This uncertainty adds a corresponding measure of difficulty to the estate planning of individuals who may be impacted by these taxes. Broadly speaking, those individuals fall into two categories:

1. Category 1. We are most concerned about individuals who die in 2010 before Congress changes the law and whose estates may therefore be subject to the 2010 rules as they presently exist. We are particularly concerned about clients who have estate planning documents that make reference to potentially obsolete law. Such references may include terms like the "marital deduction," the "federal estate tax," the "unified credit," the "estate tax exclusion" or "exemption" amount, the "credit equivalent" amount, the "credit shelter" amount or the "generation-skipping transfer tax exemption." While no one can predict when a person will die, some of our clients may have more exigent reasons for ensuring that their estate plans correctly reflect their intent. **If you know or advise someone who may fall into this category, please contact us as soon as possible.** The following are a few examples of how the current tax environment may cause problems for those who die with estate plans based on prior law:

(a) Disposition Based on Estate Tax Exclusion. For some couples, the estate plan envisions passing an amount equal to the estate tax exclusion directly to children or other beneficiaries, and not to the surviving spouse, or including children or other individuals with the spouse as beneficiaries of a trust holding the exclusion amount. Such plans may now inadvertently pass the entire estate in that manner because the estate tax exclusion is essentially unlimited. It is important to revisit these plans and ensure they correctly reflect the couple's intent.

(b) Disposition Based on Generation-Skipping Tax Exemption. In some cases, an estate plan envisions an allocation of assets among classes of beneficiaries (for example, children and grandchildren) based on the amount of the so-called generation-skipping tax exemption. Like the estate tax exclusion, that exemption is now unlimited. Depending on how an estate plan is drafted, an allocation of an amount equal to the exemption could dispose of the entire estate, thereby cutting out other important beneficiaries.

(c) Income Tax Basis of Inherited Assets. Under the law in effect before January 1, 2010, the income tax basis of an inherited asset -- that is, the value from which gain or loss is measured when an inherited asset is later sold or exchanged -- was normally its fair market value at the death of its former owner. However, under the law applicable to deaths in 2010, a deceased owner's income tax basis will largely "carry over" to the individuals who inherit his or her assets, with the following adjustments: there will be a $1.3 million "step-up" in basis available to heirs generally and an additional $3 million "step-up" in basis for property left in certain ways to a surviving spouse. Existing estate plans generally do not address the allocation of such basis among the beneficiaries of the estate, so the allocation is left to the discretion of the executor. However, because executors often are beneficiaries of the estates they administer, this may create a conflict that some clients may prefer to avoid. Such a conflict could be avoided by appointing an independent executor to make the allocation or by specifically directing how the allocation should be made.

Of course, the above examples are only a few of the problems that could arise for individuals who die while the current law is in effect but with estate planning documents based on prior law. **Again, if you know or advise someone who may fall into this category, please contact us as soon as possible.**

2. Category 2. The second category consists of all others – that is, those who are not expected to die before Congress changes the law but who may be inclined to consider taking advantage of certain aspects of the 2010 law. For this category of individuals, it is reasonable to delay changing estate planning documents until there is certainty regarding the law. However, when Congress passes a new law (or in 2011 if Congress does not act before then), individuals in this category will have to confront issues similar to those discussed above, and it will be important to revisit estate plans making reference to prior law to ensure they correctly reflect the parties' intent.

In addition and perhaps more importantly, the current tax environment may present lifetime planning opportunities for individuals in both categories. Because the highest gift tax rate has been reduced to 35% and because the generation-skipping tax has been repealed, it may be possible to reduce or eliminate the tax that otherwise would be incurred by making certain types of structured transfers now. If you or anyone you advise is interested in exploring techniques that may be employed to take advantage of the favorable transfer tax environment, please contact us.

We stand ready to work with you, your other advisors and those you advise to consider the impact of these circumstances and to assist you in the important planning that takes them into account. If we can be of assistance, please contact your HTT&S attorney.

Sincerely Yours,

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